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Tax Features

Foundation Seminar Examines Tax Policy's Impact on Economic Growth

Over one hundred tax executives, congressional staff members and Administration officials gathered May 22nd in Washington, D.C. for the Tax Foundation's seminar "Rebuilding the U.S. Industrial Base: The Role of Tax Policy."

James C. Miller III, co-chairman of the Tax Foundation and former Director of the Office of Management and Budget under President Reagan, introduced keynote speaker Lawrence

Lawrence B. Lindsey, special assistant to the President for economic policy development, and a Federal Reserve Board nominee, leaves the seminar surrounded by reporters after his keynote address.

B. Lindsey, special assistant to the President for domestic economic policy, with an admonition to the press that his remarks had to be off the record due to his pending confirmation to the Federal Reserve Board.

The first panel on pro-growth tax policies, moderated by economist Leif H. Olsen, included speeches by Congressman Richard T. Schulze (R-PA), William C. Dunkelberg of Temple University, and Charles Hahn of Dow Chemical Company.

The second panel on U.S. tax policies' impeding transborder investment was chaired by Catherine Porter of Miller & Chevalier. Speakers included Alan J. Lipner of American Express Company, Marlin Risinger from the Treasury Department, Edmund K. Harding of Xerox Corporation, and George N. Carlson of Arthur Andersen & Co.

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FRONT BURNER

Bring Order to Research and Development Tax Policy

Senator John Chafee

Concern about the ability of U.S. businesses to compete with foreign firms has been increasing in recent years. International competitiveness has become one of the top concerns of Congress, and rightly so. Given the importance of this issue, government policies, especially tax policies, should be carefully scrutinized to ensure they do not hinder our ability to compete.

One area of tremendous importance in today's competitive environment is research and development (R&D) which leads to technological innovation. Since 1929, more than two-thirds of our economic growth has resulted from technological innovation. The nations winning the competitiveness race are those that recognize the importance of advanced technology — because it results in new marketable products and more efficient production and manufacturing. These countries work to attract companies that will establish research and development facilities within their borders.

To achieve greater economic competitiveness we must not impede U.S. investment in research and development. With this goal in mind, Senator Baucus and I are introducing legislation to help U.S. business regain its competitive edge. Our bill will change a tax policy which actually impedes our ability to compete, and may, in fact, encourage the export of R&D activities and important technological advances.

Yet, the U.S. is falling behind in its development of new technologies. One of the reasons for this decline is the research allocation rules contained in Treasury Regulation Section 1.861-8, issued in 1977. This is confirmed by a

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Senator John Chafee, Republican from Rhode Island, serves on the Senate Finance Committee.

The opinions expressed in the Front Burner are not necessarily those of the Tax Foundation. Editorial replies are encouraged.

Tax Foundation

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recommendation in a report by the Council on Competitiveness to "place a permanent moratorium on Treasury Regulation 1.861-8, . . . This regulation increases the effective rate of U.S. taxation of R&D in the United States."

"Stable tax policies with regard to research and development are extremely important. Without stability, we cannot expect our major investors in R&D to make the long-range plans that are critical to some of our most promising research efforts."

The 861-8 regulations require U.S. companies with foreign operations to allocate a portion of their domestic R&D to their foreign income. Of course, foreign countries do not allow our companies to use the cost of research performed in the U.S. as a deduction from the income earned in the foreign country. The net effect is to increase the worldwide tax liability of the companies performing R&D in the U.S., encouraging American companies to locate their R&D efforts abroad.

While the regulations may be founded on what some would consider valid technical tax principles, it is difficult to understand why the United States would adopt policies that discourage the pursuit of domestic R&D. Shortly after the regulations were issued, Congress recognized that they represented poor tax policy and placed a moratorium on their implementation. Congress has renewed this moratorium seven times. It's time to put an end to the controversy surrounding Section 861 — over a decade of uncertainty is enough.

Stable tax policies with regard to research and development are extremely important. Without stability, we cannot expect our major investors in R&D to make the long-range plans that are critical to some of our most promising research efforts. With permanent reform of Section 861, we have an opportunity to both change a misguided policy and to increase long-term R&D investment.

Efforts to reform Section 861 have often been misinterpreted. It has been alleged that reform is some type of tax break — I assure you that is not the case. Section 861 is a penalty on domestic R&D, because it requires U.S. R&D performers to engage in an accounting fiction that leads to double taxation and increases their worldwide tax liability. Removal of this penalty simply allows American companies to be treated like their counterparts all over the world.

It has also been alleged that reform of section 861 will only benefit multinational corporations. In a way, this is true — a U.S. company must have foreign operations in order to be penalized by Section 861. However, small companies that conduct U.S. R&D and sell abroad are also penalized by Section 861, just like the larger corporations. There are hundreds of small companies that will be burdened less, and made stronger and more competitive, if the section 861 penalty is removed.

"Shortly after the regulations were issued, Congress recognized that they represented poor tax policy and placed a moratorium on their implementation. Congress has renewed this moratorium seven times. It's time to put an end to the controversy surrounding Section 861 — over a decade of uncertainty is enough."

Fortunately, President Bush has led the way toward settling this issue with a proposal to extend the current moratorium for one additional year. However, the President's proposal does not go far enough. These pro-competitive policies must be made permanent to encourage new technological innovation by our companies, to improve American tax policy, and promote American competitiveness.

Property Taxes Up $10.3 Billion in FY'89, Hitting $142.5 Billion

State and local property tax revenues increased $10.3 billion in fiscal year 1989, up 7.8 percent from FY'88. This collection of $142.5 billion in property taxes in 1989 is more than double the $65 billion collected a decade ago, and revenues from property taxes currently represent over 30 percent of total state/local revenues.

This decade of prodigious increases has spurred taxpayers in some states to demand lower property taxes, though the relief has often been accompanied by individual and corporate income tax hikes. Compared to the 7.8 percent growth rate in property taxes in FY'89, individual and corporate taxes rose 10.7 percent and 9.2 percent respectively.

Major Source of Local Revenues

Property tax remains the leading tax revenue source for local governments, providing 74 percent of the FY'89 total. Local property tax revenue rose $9.9 billion from FY'88 to FY'89, reaching a total of $137 billion for 1989. Although forty-eight states impose some type of property tax, the levies apply to a narrow base and furnish under 2 percent of total state monies. While the other eight states do not impose a property tax, their localities levy property taxes that provide an average of 27 percent of total state and local tax revenues.

Growth Per Capita and Per $1,000 of Personal Income

While total property tax revenues have grown by 119 percent over the past ten years from $65 billion to $142.5 million, per capita growth in property taxes has risen at a slower rate, 95 percent, from $295 in 1979 to $574 in 1989. When related to personal income, property taxes per $1,000 of personal income have declined slightly, from $38 to $35 per $1,000 of personal income.

Per Capita

Taxpayers in four states and the District of Columbia paid over $1,000 each in property taxes in 1989. States

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with the highest per capita burden are Alaska ($1,257), District of Columbia ($1,177), New Hampshire ($1,058), New Jersey ($1,056), and Connecticut ($1,003). States with the lowest per capita property tax burden were Alabama ($148), New Mexico ($180), Arkansas ($211), Kentucky ($228), and West Virginia ($237). Residents with the highest per capita property tax collections paid an average of $909 more than citizens in the lowest per capita states.

Property Tax Collections by State

Per Capita and Per $1,000 of Personal Income

Fiscal Years 1979 and 1989

	Per Capita Property Tax				Property Tax Per $1,000 of Pers. Income			
	Amount		Percent	Rank	Amount		Percent	Rank
State	1979	1989	Change	1989	1979	1989	Change	1989
Total	$295	$574	94.6%	-	$38	$35	-7.5%	-
Alabama	73	148	104.1	51	12	12	-0.4	51
Alaska	826	1,257	52.2	1	76	66	-12.8	1
Arizona	353	600	70.0	23	50	41	-18.1	19
Arkansas	125	211	68.0	49	21	17	-17.3	48
California	266	543	104.0	27	30	30	-2.1	33
Colorado	326	635	94.6	19	42	39	-7.3	22
Connecticut	456	1,003	119.8	5	51	44	-15.4	15
Delaware	165	276	67.1	44	19	16	-17.6	49
Florida	247	549	122.3	24	34	34	1.0	27
Georgia	209	444	111.8	33	31	30	-6.2	34
Hawaii	191	335	75.9	39	23	20	-13.3	43
Idaho	245	386	57.5	37	36	31	-14.4	31
Illinois	350	657	88.1	18	39	38	-4.3	23
Indiana	247	480	94.6	30	32	32	0.6	29
Iowa	339	624	84.1	20	42	43	0.5	17
Kansas	357	617	72.6	21	46	39	-13.8	21
Kentucky	131	228	74.8	48	20	18	-10.6	47
Louisiana	102	241	137.8	46	15	20	27.6	46
Maine	303	666	120.2	16	48	45	-7.4	13
Maryland	276	546	97.8	25	33	28	-13.9	36
Massachusetts	546	743	36.1	10	69	36	-47.9	24
Michigan	376	764	103.3	9	44	46	4.3	11
Minnesota	311	659	111.8	17	40	40	0.3	20
Mississippi	138	291	111.7	43	25	26	4.3	38
Missouri	205	318	54.9	41	28	21	-26.5	42
Montana	408	679	66.4	15	61	53	-12.7	6
Nebraska	389	698	79.4	14	52	47	-7.9	10
Nevada	355	386	8.8	36	40	23	-41.9	39
New Hampshire	426	1,058	148.5	3	59	56	-5.8	3
New Jersey	506	1,056	108.7	4	58	48	-16.7	9
New Mexico	131	180	37.0	50	20	15	-28.5	50
New York	482	929	92.9	6	58	48	-17.2	8
North Carolina	163	322	97.7	40	25	23	-8.4	40
North Dakota	257	441	71.4	34	36	34	-5.9	26
Ohio	260	476	83.0	31	33	31	-6.9	32
Oklahoma	149	267	78.9	45	21	20	-5.1	45
Oregon	366	795	117.4	8	47	54	16.5	4
Pennsylvania	230	467	103.4	32	30	29	-2.5	35
Rhode Island	399	737	84.7	11	53	44	-17.3	14
South Carolina	151	353	134.3	38	24	28	14.8	37
South Dakota	343	544	58.7	26	50	43	-14.3	16
Tennessee	155	296	90.9	42	24	22	-9.6	41
Texas	274	613	123.8	22	36	42	16.4	18
Utah	230	420	82.1	35	37	35	-5.3	25
Vermont	360	729	102.4	12	56	48	-12.8	7
Virginia	223	541	142.7	29	29	31	5.8	30
Washington	308	542	76.0	28	38	34	-10.6	28
West Virginia	131	237	81.7	47	20	20	0.5	44
Wisconsin	346	710	105.2	13	46	46	-1.1	12
Wyoming	513	870	69.6	7	63	63	0.4	2
Dist. of Columbia	323	1,177	263.8	2	32	54	69.7	5

Source: Department of Commerce; and Tax Foundation computations.

In terms of the decade's growth rate in per capita property taxes, nineteen states and the District of Columbia more than doubled their collections. The District of Columbia led the nation with a 264 percent growth rate, with New Hampshire and Virginia following behind at 149 percent and 143 percent respectively. None of the fifty states reported a decline in per capita property collections between 1979 and 1989.

Per $1,000 of Personal Income

When comparing property taxes per $1,000 of personal income, Alaska ($66), Wyoming ($64), and New Hampshire ($56) led states with the highest collections. The lowest property tax burdens by this yardstick were in Alabama ($12), New Mexico ($15), and Delaware ($16).

Between 1979 and 1989, thirteen states and the District of Columbia experienced increases in property taxes in relation to personal income. The District of Columbia reported the largest increase of 70 percent, from $32 in 1979 to $54 in 1989. Massachusetts and Nevada realized the sharpest reduction in the property tax/income ratio during the decade, down 48 percent and 42 percent respectively.

This decade of prodigious increases has spurred taxpayers in some states to demand a lighter property tax burden, though the relief has often been accompanied by individual and corporate income tax increases.

Outlook

A recent Tax Foundation survey of the fifty states revealed that many states are re-examining property taxes. Kansas, Michigan, New Jersey, Oregon, and Wisconsin have already placed property tax reform at the top of their FY'92 agenda. Many reforms are efforts by the states to balance the increase in other taxes. Taxpayers may witness reforms in property taxes for FY'92, which would include tax relief plans in the form of credits and rate reductions. ■

Uniform Business Tax Would Revamp U.S. Corporate Taxes

On April 30, 1991, Tax Foundation economist Paul G. Merski interviewed Congressman Richard T. Schulze on his proposal for a Uniform Business Tax which would replace the current corporate income tax and the employer portion of the Social Security tax with a nine percent tax on business receipts less the cost of goods sold.

In the tradition of the Foundation's serving as a forum for objective debate on key tax policy issues, business leaders from a cross-section of American industry respond to the congressman's proposal on page 6.

Q Currently, there seems to be a consensus that the U.S. corporate tax system has become the most complex in the world and costs almost as much to comply with as it raises in revenues. What is the "Schulze Solution" and will it simplify our complex corporate tax system?

A There are several excellent studies which show that it costs the business community almost as much to maintain tax records and fill out corporate tax forms, as is raised in revenues. One several years ago showed definitively a cost of $.66 for each dollar collected. Since that time we've had the Tax Reform Act of 1986, we've had TEFRA, DEFRA, OBRA, COBRA, TAMRA, OBRA II — a virtual alphabet soup of so-called tax reform or tax revisions. Unfortunately, if anything, the tax code has become much more complex. My answer to this problem is the Uniform Business Tax, or UBT, and one of my goals with the proposal is simplification. As a matter of fact, what we're striving for is to greatly reduce the $90-100 billion it now costs corporate America — the business community — just to comply with the corporate income tax. What I would like to see is a tax system that would eliminate this huge dead-weight cost of tax compliance and administration both for the government and the business community.

Q Taxpayers, as you pointed out, have already witnessed 14 major tax bills enacted over the past decade, and yet we are still facing record budget deficits. How would your Uniform Business Tax legislation address the deficit without increasing the record high tax burden on the American taxpayer?

A The Uniform Business Tax will not increase the tax burden on American taxpayers. The UBT will substitute a flat 9 percent tax on gross receipts less the cost of goods sold for the existing corporate income and payroll tax. Our goal is to raise just about the same amount as corporations now pay. The border aspects, or the territorial aspects, of this tax, however, being collected at the border and rebated on goods sold overseas, would bring in approximately $50 billion of additional revenues, which could make a meaningful contribution toward deficit reduction.

Congressman Richard T. Schulze (right), a member of the House Ways and Means Committee, is interviewed by the Tax Foundation's director of fiscal affairs, Paul G. Merski.

Q The idea of implementing a value-added type tax has been around for decades but has never received much support from the business community. How does your UBT differ from a value-added tax?

A I'm glad you asked that question because it's very difficult trying to explain that the UBT is not a VAT. In one of the brochures we send to people who ask us about it, we have made up a list of comparisons between the VAT, the UBT, and the corporate income tax. I will try to briefly compare the VAT with the UBT. Let me first say that one of our major goals was, and is, tax simplification. With a standard European type VAT, at every level of production there is an additional tax, an additional transaction, paperwork, taxes paid, credits given, slips back and forth, audits called for — it is extremely complex. Or let me turn that around and say, it is complexity in the extreme. One of the cries against a standard European style VAT has historically been its complexity. My proposal will hopefully achieve the other extreme of simplicity. That is a major difference between the VAT tax and the UBT. Normally, a VAT, when applied, is added on top of existing taxes. The UBT would not be added, but would be used in place of existing taxes. It is not a multi-staged sales tax like the VAT. I believe that the business community would pay this tax, which is paid in

total at the end, rather than a standard add-on European type VAT. Even in retail stores they have the price plus a VAT and so it's very obvious that it's added on top. I think the UBT is not only simpler, but it's not passed on totally to the consumer. So two of the key differences between them are the incidence of the tax and the method of calculation. The difference between a credit for a VAT and a deduction from the UBT is a large difference and I think that it makes the UBT much preferable.

Q Given our global economic environment, the impact that U.S. tax policies have on transborder investment cannot be ignored. How would the UBT impact our competitiveness with major trading partners, and is it consistent with international taxation practices?

A It certainly is consistent with international tax practices and that's been one of our major objectives. The UBT is a GATT-legal tax which has a high degree of consistency with our major trading partners without really changing our entire structure and making it like the European type system. The border applicability of this tax makes it dovetail very well with all of our major trading partners, all of whom have some form of border tax or territorial tax. So in international trade, it has a tendency to level the playing field. Products made in the United States today have built into them all of the costs of government: local, state, and federal government, through the various taxes that are paid by the producers. When these products are shipped, for instance, to a European country, as it crosses the border, the cost of their government is added to that product so that not only is the cost of our government involved in the product, but the cost of the ultimate user country is included as well. When that same product is made in a European country and shipped to the United States, the tax which has been paid is rebated and, as a consequence, their cost of government is not involved. As it comes across the border our cost of government is not placed into it, which puts us at an economic and competitive disadvantage. And so I think that the UBT is not only consistent with our international obligations and the practices of our trading partners, but helps the domestic producer.

Q A common complaint of U.S. manufacturers is the high cost of capital relative to other industrialized nations. Would your UBT help reduce capital investment costs here in the U.S.?

A My belief is that it will allow a dramatic reduction in the cost of capital because the UBT allows immediate expensing of capital goods. Our goal is to lower the cost of capital and, in fact, put an incentive in for expansion, modernization, and improving plant facilities and productivity. I think we can achieve that with the UBT.

Q Many taxpayers fear that new tax legislation automatically translates into higher taxes. Your UBT legislation plans to raise an additional $50 or $60 billion per year — does that mean higher taxes and increased government spending?

A I'm convinced that it will not mean higher taxes and higher spending. There exists a transfer pricing problem in our country when some foreign corporations operating in the U.S. are making inordinate profits at home and avoiding paying taxes in the United States. The border aspects of the UBT would cure a portion of the transfer pricing problem. If products coming into America now have been over-priced somewhat, or their prices are not in line with other markets elsewhere, the difference will be absorbed immediately by the shipping country or company with little impact on the domestic prices. In my opinion, in a competitive environment, the tax would not be passed on to domestic consumers, but would be mainly paid by foreign corporations and companies.

Q In addition to replacing the corporate income tax, the UBT also replaces the existing employer-paid portion of the FICA payroll tax. Will this aspect jeopardize revenues going into the Social Security Trust Fund?

A That was the first question the AARP (American Association of Retired Persons), who keep a very close eye on such things, asked when we sat down with them and explained the UBT. We explained to them that the employers' portion of FICA will be paid in a preferential manner just as it is today. That seemed to satisfy them, and the answer is that it will not make any change in the way FICA is handled.

Q With such a broad-based tax as the UBT, what would prevent the government from extracting huge amounts of additional revenue simply by raising the rate 1 or 2 percent every few years above the 9 percent you have outlined?

A That's always been a fear with any tax, and I think, quite frankly, a justifiable one with today's budget situation and tax structure. Because our current corporate tax code is so complex, we tend to pick winners and losers and can pick off the industries and portions of industries to tax. With the UBT's broad-based relatively flat system, you would impact every business entity in the United States, large and small, if you were to make a change. I don't think that would be done either lightly or easily. As a matter of fact, I think it would pose one of the most difficult political problems for anyone who thought they could raise this tax in a cavalier off-hand manner. Therefore, I think just the opposite — that it would be an extremely difficult tax to increase.

Q What reaction has the UBT received from your colleagues here on Capitol Hill and from the business community around the nation?

A As with any tax proposal, the initial reaction is skepticism. But as we respond to concerns, take a closer look at the numbers, and view the product with a careful eye on what a tax structure should do to set sound tax policy, we're getting more and more acceptance. The proposal is not hard to understand or complicated, but the standard reply from many businesses, after what they've been through for the last decade and a half, is, "No, don't change anything." But when we sit down with them and discuss where we're going as a nation, how we're going to get there, what their vision of the United States is in a very competitive world, the UBT becomes more attractive. It's really a question of whether we're going to be able to compete in a global economic environment, not only in the service industries, but in manufacturing as well. We're getting more and more of the reaction of Lee Iacocca, chairman of Chrysler, for instance, who thinks that it's imperative that we make such a change and put sound tax policies in effect. ■

Tax Policy Community Responds to the Uniform Business Tax

The UBT: A VAT By Any Other Name

Michael Altier
Vice President & Legislative Counsel
National Retail Federation

Congressman Schulze has distributed among various business groups a proposal calling for a 9 percent Uniform Business Tax (UBT) that would replace the current business income taxes and the employer's portion of the FICA payroll tax.

Although proponents of the UBT wish to characterize it as a revamped border-adjustable business tax system, we at the National Retail Federation believe the UBT is a form of value-added tax, and in recent House Ways and Means Committee hearings, Members referred to "border-adjustable taxes" and

We believe the UBT is a form of value-added tax . . . . [its] disadvantages are as valid today as they were twenty years ago . . . regressivity, inflationary impact, and potential complexity.

"value-added taxes" interchangeably. Thus, we must presume that any legislation in this area will be a variation of a value-added tax.

Over the years, retailers have consistently opposed various forms of a value-added tax, and its disadvantages are as valid today as they were twenty years ago. These include regressivity, inflationary impact, and potential complexity.

Congressman Schulze points to the UBT's qualification as a border-adjustable tax under GATT as a major advantage. This characteristic would seem to encourage exports while making imports more expensive. Additionally, the UBT claims to export $60 billion of tax liability to foreign entities while leaving the U.S. business taxpayer's liability revenue neutral. We find it hard to believe that foreign suppliers will absorb such a significant tax increase — most of the additional cost on imports will be passed through to the consumer.

The UBT is a radical proposal in terms of changing a tax system that has evolved over the last 70 years. We maintain that until sufficient economic studies and other testing of such a proposal can be done to determine the true impact on the U.S. economy, such a proposal is extremely dangerous and cannot be endorsed. Although the current tax system does have its faults and complexities, it has served the country well. This is not to say that changes are not warranted, but let us first try to work within a system where the economic outcome is more predictable.

The UBT: Faimess and Simplification in One

George T. Esherick
Vice President, Government Relations
American Iron and Steel Institute

Congressman Schulze's UBT proposal is a good addition to the debate over constructing a more competitive U.S. tax system. To be competitive in the 1990s and beyond, the U.S. needs fiscal policies that address the anti-competitive nature of our present business tax system. To accomplish this, we need to totally reform the way in which commerce is taxed in the U.S. As such, the American Iron and Steel Institute favors the consideration of a broad based border-adjustable tax as a substitute for the current business tax system and as a vehicle for providing investment and

[We] favor the consideration of a broad based border-adjustable tax as a substitute for the current business tax.

savings incentives. Such a tax would be levied on imports and rebated on exports, thus improving the competitiveness of domestically produced goods both in the U.S. and overseas markets.

A properly constructed, border-adjustable tax would create a broader and fairer tax system which would also be less complicated. It would help enhance U.S. savings and investment; not disadvantage one industry or region over another; be revenue neutral for all U.S. taxpayers; simplify the tax code; and hold promise to reduce the federal budget deficit without further eroding U.S. competitiveness.

Be Wary of Trading Taxes

Norman B. Ture
President
Institute for Research on the Economics of Taxation

In the abstract, the UBT — a subtraction-method value added tax — is superior to the existing business income taxes in many important respects. It is neutral in its effect on the use of production capability for capital formation compared with consumption and with respect to the use of labor and capital services in production. Because the UBT would apply only to value added originating in domestic production, its replacement of business income taxes would contribute

The UBT would present a very great risk of accelerating growth in federal spending.

to improving the competitive position of American businesses in the world market place.

The most important function of a tax is to inform the citizens about the cost of government. To perform this function effectively, a tax must be imposed directly on the largest possible number of real persons. Taxes on business entities fail this test because their burden is hidden from the real people who ultimately pay them. In this respect, the UBT would be no better than the corporate income tax it is intended to replace. Because the UBT would also be a much more potent revenue raiser that business income taxes, its adoption would present a very great risk of accelerating growth in federal spending, thereby canceling any economic benefits it might otherwise provide. We should eliminate the corporate income tax but not by substituting for it another tax that in practice might well be more harmful to economic efficiency, growth, and competitiveness.

Seminar from page 1

Rejuvenating service sector strength was the theme of the third panel. Emil M. Sunley of Deloitte & Touche moderated and introduced Thomas S. Neubig of Price Waterhouse, Henry Ruempler of the American Bankers Association, and Jane G. Gravelle of the Congressional Research Service.

Proceedings of the seminar will be available soon. Please contact the Foundation if you are interested.

Economist Leif H. Olsen finds the literature on the capital gains tax excessively absorbed with one question: Will a higher or lower rate produce more revenue? The more important issue to Olsen is its effect on capital formation and growth.

Congressman Richard T. Schulze holds up a Uniform Business Tax form which would replace the current, much more complex corporate tax return should his idea of a uniform business tax be proposed and enacted. Professor William Dunkelberg of Temple University looks on.

Catherine Porter, partner in the law firm of Miller & Chevalier, presided over a lively exchange on the wisdom of the subpart F rules.

FOUNDATION MESSAGE

U.S. High-tech Competitiveness and The R&D Tax Credit

Dan Witt
Executive Director

The last half of the 1980s was a great disappointment to Americans who see research and development (R&D) as vital to the nation's economy. Real growth in R&D expenditures only averaged 1.3 percent from 1985 to 1988, and suffered a 0.9 percent decrease in real growth during 1989, the first such decline in 14 years. This stagnant period contrasts sharply with the first half of the decade when R&D expenditures increased an average of 8.2 percent in constant dollars. The U.S. currently spends substantially less than either West Germany or Japan on non-defense R&D.

What role has tax policy played in this nosedive? What provisions of our tax code provide corporations with positive incentives to invest in research and development? Which provisions of the code inhibit R&D expenditures? Everyone here in Washington seems to agree on the benefits to our economy of more R&D. But despite this unanimity, the U.S. R&D tax credit has been since its inception in 1981 a jumble of short-term extensions and technical changes to its calculation that has not provided substantial incentive for U.S. firms to increase R&D expenditures.

A parallel and possibly related trend is the decline the U.S. is experiencing in its share of global sales of technology-intensive products. Tax Foundation senior research fellow B. Anthony Billings will soon publish a study on R&D intensity that examines its sensitivity to the R&D tax credit, changes in the corporate statutory tax rate, and changes in the corporate tax base.

On the political front, the R&D tax credit is in limbo with the rest of the "extenders"—tax provisions that must be reauthorized, or extended, every year. In judging which provisions should be subject to this reauthorization procedure, the R&D tax credit seems ill-suited. Since R&D projects that qualify for the credit are planned over a period of several years, the stimulus the credit provides is lessened by the uncertainty of its application in future years. A permanent credit, or at least a multi-year extension, would be a small but worthwhile step towards a more stable and reliable tax code, and possibly a boost to U.S. competitiveness.

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- **3M Company**
- **United Parcel Service Inc.**
- **Vulcan Materials Company**
- **Warner-Lambert Company**

Tax Freedom Day Analysis Brings Media to Foundation's Door

The publication of Tax Foundation's Tax Freedom Day Special Report last month brought more attention to the Foundation's public information program than any previous year's announcement of Tax Freedom Day.

The Foundation's executive director Dan Witt talks about the growing tax burden across the nation on the Radio America network.

Most of the new demand for Tax Foundation information came from the states, as the second year of the Foundation's calculation of a state-by-state Tax Freedom Day spurred interest in how each state's tax burden compared with those of neighboring states.

From April 24, the date of the nation's earliest Tax Freedom Day in Mississippi, until May 26 when the taxpayers of New York and the District of Columbia had finally earned enough to pay for government, the Foundation's staff did radio interviews in over 30 states.

An important benefit of this attention is the media's greater reliance on the Foundation for economic analysis on other issues. Paul Merski, the Foundation's director of fiscal affairs, spoke on Maryland's fiscal situation at a conference entitled *Maryland Tax Policy: Who Pays and Who Benefits.* He was joined on the panel by noted federal budget authority Allen Schick, Director of the University of Maryland's Bureau of Government Research. Also speaking were Marcia Howard of the National Association of State Budget Officers, Hal Hovey, State Policy Research, and Steven Gold of the Center for the Study of the States. ■

Foundation Releases 1990 Annual Report

The Tax Foundation's annual report, just released, explains the mission of the Foundation and gives highlights of its accomplishments during 1990. Research, membership activities, publications, and media coverage are presented, along with messages from the Foundation's co-chairmen, James C. Miller III and James Q. Riordan, and its executive director, Dan Witt.

Paul Merski is interviewed by the CNN television network after a record-setting sale of Treasury bonds.

Tax Features

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